

SAN DIEGO COUNTY

Audit Report

SERIOUSLY EMOTIONALLY DISTURBED PUPILS: OUT-OF-STATE MENTAL HEALTH SERVICES PROGRAM

Chapter 654, Statutes of 1996

July 1, 2001, through June 30, 2005



JOHN CHIANG
California State Controller

November 2007



JOHN CHIANG
California State Controller

November 14, 2007

Tracy Sandoval
Assistant Chief Financial Officer/Auditor-Controller
San Diego County
1600 Pacific Highway, Room 166
San Diego, CA 92101

Dear Ms. Sandoval:

The State Controller's Office audited the costs claimed by San Diego County for the legislatively mandated Seriously Emotionally Disturbed Pupils: Out-of-State Mental Health Services Program (Chapter 654, Statutes of 1996) for the period of July 1, 2001, through June 30, 2005.

The county claimed \$9,933,677 (\$9,935,677 less a \$2,000 penalty for filing late claims) for the mandated program. Our audit disclosed that \$7,647,539 is allowable and \$2,286,138 is unallowable. The unallowable costs resulted primarily from the county claiming ineligible vendor payments for out-of-state residential placement of seriously emotionally disturbed pupils in facilities that are owned and operated for profit. The State paid the county \$1,618,908. Allowable costs claimed exceed the amount paid by \$6,028,631.

If you disagree with the audit findings, you may file an Incorrect Reduction Claim (IRC) with the Commission on State Mandates (CSM). The IRC must be filed within three years following the date that we notify you of a claim reduction. You may obtain IRC information at CSM's Web site, at www.csm.ca.gov (Guidebook link); you may obtain IRC forms by telephone, at (916) 323-3562, or by e-mail, at csminfo@csm.ca.gov.

If you have any questions, please contact Jim L. Spano, Chief, Mandated Cost Audits Bureau, at (916) 323-5849.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

JVB/wm

cc: Gil Enriquez, Senior Accountant
San Diego County
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Audit Report

Summary

The State Controller's Office (SCO) audited the costs claimed by San Diego County for the legislatively mandated Seriously Emotionally Disturbed Pupils: Out-of-State Mental Health Services Program (Chapter 654, Statutes of 1996) for the period of July 1, 2001, through June 30, 2005. The last day of fieldwork was September 6, 2007.

The county claimed \$9,933,677 (\$9,935,677 less a \$2,000 penalty for filing late claims) for the mandated program. Our audit disclosed that \$7,647,539 is allowable and \$2,286,138 is unallowable. The unallowable costs resulted primarily from the county claiming ineligible vendor payments for out-of-state residential placement of seriously emotionally disturbed (SED) pupils in facilities that are owned and operated for profit. The State paid the county \$1,618,908. Allowable costs claimed exceed the amount paid by \$6,028,631.

Background

Chapter 654, Statutes of 1996, added and amended Government Code section 7576 by allowing new fiscal and programmatic responsibilities for counties to provide mental health services to SED pupils placed in out-of-state residential programs. Counties' fiscal and programmatic responsibilities including those set forth in California Code of Regulations section 60100 provide that residential placements for a SED pupil may be made out-of-state only when no in-state facility can meet the pupil's needs.

On May 25, 2000, the Commission on State Mandates (CSM) determined that Chapter 654, Statutes of 1996, imposed a state mandate reimbursable under Government Code section 17561 for the following:

- Payment of out-of-state residential placements for SED pupils;
- Case management of out-of-state residential placements for SED pupils. Case management includes supervision of mental health treatment and monitoring of psychotropic medications;
- Travel to conduct quarterly face-to-face contacts at the residential facility to monitor level of care, supervision, and the provision of mental health services as required in the pupil's Individualized Education Plan; and
- Program management, which includes parent notifications, as required, payment facilitation, and all other activities necessary to ensure a county's out-of-state residential placement program meets the requirements of Government Code section 7576.

The program's parameters and guidelines establish the state mandate and define reimbursement criteria. CSM adopted the parameters and guidelines on October 26, 2000. In compliance with Government Code section 17558, the SCO issues claiming instructions, to assist local agencies and school districts in claiming mandated program reimbursable costs.

Objective, Scope, and Methodology

We conducted the audit to determine whether costs claimed represent increased costs resulting from the Seriously Emotionally Disturbed Pupils: Out of State Mental Health Services Program for the period of July 1, 2001, through June 30, 2005.

Our audit scope included, but was not limited to, determining whether costs claimed were supported by appropriate source documents, were not funded by another source, and were not unreasonable and/or excessive.

We conducted the audit according to *Government Auditing Standards*, issued by the Comptroller General of the United States, and under the authority of Government Code sections 12410, 17558.5, and 17561. We did not audit the county's financial statements. We limited our audit scope to planning and performing audit procedures necessary to obtain reasonable assurance that costs claimed were allowable for reimbursement. Accordingly, we examined transactions, on a test basis, to determine whether the costs claimed were supported.

We limited our review of the county's internal controls to gaining an understanding of the transaction flow and claim preparation process as necessary to develop appropriate auditing procedures.

Conclusion

Our audit disclosed instances of noncompliance with the requirements outlined above. These instances are described in the accompanying Summary of Program Costs (Schedule 1) and in the Findings and Recommendations section of this report.

For the audit period, San Diego County claimed \$9,933,677 (\$9,935,677 less a \$2,000 penalty for filing late claims) for costs of the Seriously Emotionally Disturbed Pupils: Out-of-State Mental Health Services Program. Our audit disclosed that \$7,647,539 is allowable and \$2,286,138 is unallowable.

For the fiscal year (FY) 2001-02 claim, the State made no payment to the county. Our audit disclosed that \$1,513,381 is allowable. The State will pay allowable costs claimed that exceed the amount paid, totaling \$1,513,381, contingent upon available appropriations.

For the FY 2002-03 claim, the State made no payment to the county. Our audit disclosed that \$3,421,815 is allowable. The State will pay allowable costs claimed that exceed the amount paid, totaling \$3,421,815, contingent upon available appropriations.

For the FY 2003-04 claim, the State made no payment to the county. Our audit disclosed that \$1,755,580 is allowable. The State will pay allowable costs claimed that exceed the amount paid, totaling \$1,755,580, contingent upon available appropriations.

For the FY 2004-05 claim, the State paid the county \$1,618,908. Our audit disclosed that \$956,763 is allowable. The State will offset \$662,145 from other mandated program payments due the county. Alternatively, the county may remit this amount to the State.

**Views of
Responsible
Official**

We issued a draft audit report on September 24, 2007. Christopher P. Gilmore, Deputy Controller, responded by letter dated November 2, 2007 (Attachment), disagreeing with the audit results. This final audit report includes the county's response.

Restricted Use

This report is solely for the information and use of San Diego County, the Department of Finance, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

Schedule 1— Summary of Program Costs July 1, 2001, through June 30, 2005

Cost Elements	Actual Costs Claimed	Allowable per Audit	Audit Adjustment	Reference ¹
<u>July 1, 2001, through June 30, 2002</u>				
Ongoing costs:				
Mental health service:				
Vendor reimbursements	\$ 1,681,983	\$ 1,513,381	\$ (168,602)	Finding 1
Travel	9,170	—	(9,170)	Finding 2
Total program costs	<u>\$ 1,691,153</u>	1,513,381	<u>\$ (177,772)</u>	
Less amount paid by the State		—		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 1,513,381</u>		
<u>July 1, 2002, through June 30, 2003</u>				
Ongoing costs:				
Mental health service:				
Vendor reimbursements	\$ 4,435,695	\$ 3,422,815	\$(1,012,880)	Finding 1
Travel	15,425	—	(15,425)	Finding 2
Subtotal	4,451,120	3,422,815	(1,028,305)	
Less late filing penalty	(1,000)	(1,000)	—	
Total program costs	<u>\$ 4,450,120</u>	3,421,815	<u>\$(1,028,305)</u>	
Less amount paid by the State		—		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 3,421,815</u>		
<u>July 1, 2003, through June 30, 2004</u>				
Ongoing costs:				
Mental health service:				
Vendor reimbursements	\$ 2,158,653	\$ 1,756,580	\$ (402,073)	Finding 1
Travel	15,843	—	(15,843)	Finding 2
Subtotal	2,174,496	1,756,580	(417,916)	
Less late filing penalty	(1,000)	(1,000)	—	
Total program costs	<u>\$ 2,173,496</u>	1,755,580	<u>\$ (417,916)</u>	
Less amount paid by the State		—		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 1,755,580</u>		
<u>July 1, 2004, through June 30, 2005</u>				
Ongoing costs:				
Mental health service:				
Vendor reimbursements	\$ 1,610,182	\$ 956,763	\$ (653,419)	Finding 1
Travel	8,726	—	(8,726)	Finding 2
Total program costs	<u>\$ 1,618,908</u>	956,763	<u>\$ (662,145)</u>	
Less amount paid by the State		(1,618,908)		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ (662,145)</u>		

Schedule 1 (continued)

Cost Elements	Actual Costs Claimed	Allowable per Audit	Audit Adjustment	Reference ¹
<u>Summary: July 1, 2001, through June 30, 2005</u>				
Ongoing costs:				
Mental health service:				
Vendor reimbursements	\$ 9,886,513	\$ 7,649,539	\$(2,236,974)	
Travel	49,164	—	(49,164)	
Subtotal	9,935,677	7,649,539	(2,286,138)	
Less late filing penalty	(2,000)	(2,000)	—	
Total program costs	<u>\$ 9,933,677</u>	7,647,539	<u>\$(2,286,138)</u>	
Less amount paid by the State		(1,618,908)		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 6,028,631</u>		

¹ See the Findings and Recommendations section.

Findings and Recommendations

FINDING 1— Unallowable vendor costs

The county claimed unallowable vendor costs of \$2,236,974 for the audit period.

The overstated costs occurred because the county:

- Claimed ineligible vendor payments of \$1,979,388 (board and care costs of \$972,392 and treatment costs of \$1,006,996) for out-of-state residential placement of seriously emotionally disturbed (SED) pupils in facilities that are owned and operated for profit. The costs represent 60% of total board and care and treatment costs.
- Claimed in-state vendor costs of \$133,776 that should have been claimed under the Handicapped and Disabled Students mandate program. We allowed the eligible portion under the Handicapped and Disabled Students mandate program.
- Claimed costs related to ineligible clients of \$119,815. The county inadvertently claimed board and care costs incurred by clients past the eligibility period authorized by the County Mental Health Department.
- Duplicated treatment payments of \$3,995.

The program's parameters and guidelines, section IV.C.1., specify that the mandate is to reimburse counties for payments to service vendors providing mental health services to SED pupils in out-of-state residential placements as specified in Government Code section 7576 and California Code of Regulations, Title 2, sections 60100 and 60110.

The California Code of Regulations, Title 2, section 60100, subdivision (h), specifies that out-of-state residential placements shall be made only in residential programs that meet the requirements of Welfare and Institutions Code sections 11460(c)(2) through (3). Welfare and Institutions Code section 11460, subdivision (c)(3), states that reimbursement shall only be paid to a group home organized and operated on a nonprofit basis.

The parameters and guidelines also state that all costs claimed must be traceable to source documents that show evidence of the validity of such costs and their relationship to the state mandated program.

The following table summarizes the unallowable vendor costs claimed.

	Fiscal Year				Total
	2001-02	2002-03	2003-04	2004-05	
Ineligible placements:					
Board and care	\$ —	\$ (420,070)	\$ (205,967)	\$ (346,355)	\$ (972,392)
Treatment	(164,607)	(374,109)	(173,831)	(294,449)	(1,006,996)
Ineligible in-state costs	—	(133,776)	—	—	(133,776)
Ineligible clients	—	(84,925)	(22,275)	(12,615)	(119,815)
Duplicated costs	(3,995)	—	—	—	(3,995)
Audit adjustment	<u>\$ (168,602)</u>	<u>\$ (1,012,880)</u>	<u>\$ (402,073)</u>	<u>\$ (653,419)</u>	<u>\$ (2,236,974)</u>

Recommendation

We recommend that the county implement policies and procedures to ensure that out-of-state residential placements are made in accordance with laws and regulations. Further, we recommend that the county only claim eligible board-and-care and treatment costs corresponding to the authorized placement period of each eligible client.

County's Response

The State's position is that the County claimed unallowable vendor costs of \$2,236,974 for the audit period; and the County disputes this finding. The County specifically disputes the finding that it claimed ineligible vendor payments of \$1,979,388 (board and care costs of \$972,392 and treatment costs of \$1,006,996) for out-of-state residential placement of SED pupils owned and operated for profit. In support of its position, the State cites the California Code of Regulations, Title 2, section 60100, subdivision (h), which provides that out-of-state residential placements will be made only in residential programs that meet the requirements of Welfare and Institutions Code section 11460(c)(2) through (3). Welfare and Institutions Code section 11460(c)(3) provides that reimbursement will only be paid to a group home organized and operated on a nonprofit basis.

The County asserts that it is entitled to the entire amount claimed less the sum already paid by the State. Please see Summary of Program Costs – SED Claim – July 1, 2001, - June 30, 2005 attached hereto as Exhibit B. In support of its position, the County provides the following five arguments and Exhibits A through D attached hereto [refer to the accompanying attachment]. The first argument is primary for the claim years July 1, 2001 through June 30, 2004, and arguments 2-5 are made in the alternative. For the claim year July 1, 2004 through June 30, 2005, arguments 2-5 shall be considered primary.

The following is a summary of the county's five arguments: The entire text of its arguments is attached to this report.

1. The Court Ruling in *County of San Diego, et al. v. State of California, et al.* (Case No. 825109 Consolidated with Case No. 827845) Clearly States the Amount the State Owes the County for the Claim Years July 1, 2001 Through June 30, 2004.
2. California Law Prohibiting For-Profit Placements is Inconsistent with Both Federal Law, Which No Longer Has Such Limitation, and With IDEA's "Most Appropriate Placement" Requirements.

3. Parents can be Reimbursed When Placing Students in Appropriate For-Profit Out-of-State Facilities. County Mental Health Agencies will be Subject to Increased Litigation Without the Same Ability to Place Seriously Emotionally Disturbed Students in Appropriate For-Profit Out-of-State Facilities.
4. County Contracted with Nonprofit Out-of-State Residential Program for SED Pupils.
5. There are no Requirements in Federal or State law Regarding the Tax Identification Status of Mental Health Treatment Services Providers. Thus there are no grounds to disallow the County's Treatment Costs.

SCO's Response

The finding remains unchanged. The county's response does not address the ineligible in-state vendor costs, ineligible clients, or the duplicated treatment payments. Our response addresses each of the five arguments set forth by the county in the order identified above.

1. We believe that the audit is valid and has a legal bearing. During the discovery for the aforementioned case, the State admitted that the county filed claims in a given amount and that the State has made partial payment. Neither the State nor the court stated that the claims were final and not subject to an SCO audit pursuant to Government Code sections 12410, 17558.5, and 17561. Further, the matter is currently in appeal and, therefore, is not *res judicata*.
2. We do not dispute the assertion that California law is more restrictive than federal law in terms of the out-of-state residential placement of SED pupils; however, the fact remains that this is a state-mandated cost program and the county filed a claim seeking reimbursement from the State under the provisions of the California Code of Regulations, Title 2, section 60100.

Regarding the discussion of IDEA funds, these federal funds are not applied as an offset to claimed residential-placement vendor payments. The only portion of the county's claim that has the potential for federal reimbursement is the duplicated travel costs in Finding 2. The travel costs are included in the pool of costs used to determine the cost per unit that is, in turn, used to determine Short Doyle/Medi-Cal Federal Financing Participation funds reimbursement for eligible clients.

Regarding the discussion of local educational agencies (LEAs), we do not dispute that Education Code sections 56366.1 and 56365 do not restrict LEAs from contracting with for-profit schools for educational services. The cited Education Code sections specify that educational services must be provided by a school certified by the California Department of Education.

3. As previously stated, the county is prohibited from placing a client in a for-profit, out-of-state residential facility under the California Code of Regulations, Title 2, section 60100, subdivision (h), and Welfare and Institutions Code section 11460, subdivisions (c)(2) through (3). Welfare and Institutions Code section 11460, subdivision (c)(3), states that payment shall only be made to a group home organized and operated on a nonprofit basis. The state mandated program's parameters and guidelines do not provide reimbursement for out-of-state residential placements made outside of the regulation.
4. As noted in our response to argument 3, the county is prohibited from placing a client in a for-profit facility and the residential-placement vendor payments shall only be made to a group home organized and operated on a nonprofit basis. Based on documents the county provided us in the course of the audit, we determined that Mental Health Systems, Inc., a California nonprofit corporation, contracted with Charter Provo Canyon School, a Delaware for-profit limited liability company, to provide out-of-state residential placement services. The referenced Provo Canyon, Utah, residential facility is not organized and operated on a nonprofit basis.
5. We do not dispute that Government Code section 7572 requires mental health services to be provided by qualified mental health professionals. As noted in our response to argument 3, the county is prohibited from placing a client in a for-profit facility and the residential-placement vendor payments shall only be made to a group home organized and operated on a nonprofit basis. The unallowable treatment and board-and-care vendor payments claimed result from the county placement of clients in prohibited out-of-state residential facilities. Again, the state-mandated program's parameters and guidelines do not include a provision for the county to be reimbursed for vendor payments made to out-of-state residential placements outside of the regulation.

**FINDING 2—
Unallowable travel
costs**

The county claimed unallowable travel costs of \$49,164 for the audit period.

The county claimed travel costs on the SED pupils mandate claim that were also included in the pool of direct costs used to compute the unit rates in the county's cost report submitted to the California Department of Mental Health. Consequently, travel costs claimed on the SED pupils mandate claim were also allocated through the unit rates to various mental health programs, including the Handicapped and Disabled Students mandate claim.

The parameters and guidelines, section IV.C.3., specify that the mandate reimburses counties for travel costs necessary to conduct quarterly face-to-face contacts at the residential facility to monitor level of care, supervision, and the provision of mental health services as specified in the California Code of Regulations, Title 2, sections 60110.

The parameters and guidelines also state that all costs claimed must be traceable to source documents that show evidence of the validity of such costs and their relationship to the state mandated program.

The following table summarizes the unallowable travel costs claimed.

	Fiscal Year				Total
	2001-02	2002-03	2003-04	2004-05	
Travel	\$ (9,170)	\$ (15,425)	\$ (15,843)	\$ (8,726)	\$ (49,164)

Recommendation

We recommend that the county use a consistent cost allocation methodology to minimize any potential duplication with other mental health programs.

County's Response

The State alleges that the County has claimed unallowable travel costs of \$49,164 for the audit period July 1, 2001 through June 30, 2005. The County disputes this finding and submits the attached cost per unit calculation as Exhibit D [refer to the accompanying attachment]. This cost per unit calculation clearly indicates that the County has excluded the travel costs in calculating the cost per unit per claim to calculate the gross costs in the County's Handicapped and Disabled Student's claim. Therefore, because these costs were clearly excluded they are valid SED claimable costs in the amount of \$49,164.00.

SCO's Response

The finding remains unchanged.

We do not dispute the impact on the unit rate if the travel costs were omitted from the unit rate calculation. However, based on documentation the county provided during the course the audit, we determined that the travel costs are expensed in a pool of costs that is used to determine the cost-per-unit on the county's cost report submitted to the California Department of Mental Health. This resulted in a duplication of claimed costs because the unit costs are allocated to federal and state programs—including the Handicapped and Disabled Students mandate claim—based on the units of service, and are claimed in total on the SED pupils mandate claim.

**Attachment—
County's Response to
Draft Audit Report**



County of San Diego

DONALD F. STEUER
CHIEF FINANCIAL OFFICER
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FAX (619) 531-5219

AUDITOR AND CONTROLLER
1600 PACIFIC HIGHWAY STE 166, SAN DIEGO, CALIFORNIA 92101-2478

TRACY M. SANDOVAL
ASST. CHIEF FINANCIAL OFFICER/
AUDITOR & CONTROLLER
(619) 531-5413
FAX (619) 531-5219

November 2, 2007

Jim L. Spano, Chief
Mandated Cost Audits Bureau
California State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250-5874

Dear Mr. Spano:

RESPONSE TO SED PUPILS: OUT OF STATE MENTAL HEALTH SERVICES PROGRAM AUDIT FOR THE PERIOD OF JULY 1, 2001 THROUGH JUNE 30, 2005

The County of San Diego (County) is in receipt of the State Controller's Office draft audit report of the costs claimed by the County for the legislatively mandated Seriously Emotionally Disturbed (SED) Pupils: Out of State Mental Health Services Program for the period of July 1, 2001 through June 30, 2005. The County received the report on October 3, 2007 and received an extension from Mr. Jim L. Spano, Chief, Mandated Audits Bureau to submit its response to the report on or before November 2, 2007. The County is submitting this response in compliance with that extension on November 2, 2007.

As directed in the draft report, the County's response will address the accuracy of the audit findings. There were two Findings in the above-referenced Draft Report and the County disputes both Finding 1 - Unallowable Vendor Costs and Finding 2 - Unallowable Travel Costs. The County claimed \$9,933,677 for the mandated programs for the audit period and \$1,618,908 has already been paid by the State. The State Controller's Office's audit found that \$7,647,539 is allowable and \$2,286,138 is unallowable. The unallowable costs as determined by State Controller's Office occurred primarily because the State alleges the County claimed ineligible vendor payments for out-of-state residential placement of SED pupils in facilities that are owned and operated for profit. As stated above, the County disputes this Finding 1 and submits the attached response in support of its position. The County also disputes Finding 2 which alleges the County claimed unallowable travel costs. The County submits the attached response in support of its position with respect to Finding 2, as well. Thus, the County asserts that \$8,057,183 are allowable costs that are due the County for the audit period.

Response to SED Pupils: Out of State Mental
Health Services Program Audit for the Period of
July 1, 2001 through June 30, 2005

Page Two

November 2, 2007

If you have any questions, please contact Lisa Macchione, Senior Deputy County Counsel at
(619) 531-6296.

Sincerely,

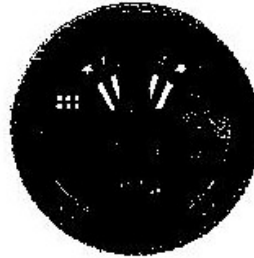
Handwritten signatures of Christopher P. Gilmore and Terry Hogan. Christopher's signature is on the left, and Terry's is on the right.

CHRISTOPHER P. GILMORE
Deputy Controller

TERRY HOGAN, Group Finance Director
Health and Human Services Agency

RCA:MF:lc

Attachments



County of San Diego's Response To
The California State Controller's
September 2007 Audit Report

**Seriously Emotionally Disturbed
Pupils: Out of State Mental
Health Services Program Audit**

For the Period July 1, 2001
through June 30, 2005

**COUNTY OF SAN DIEGO'S RESPONSE TO
SED PUPILS: OUT OF STATE MENTAL HEALTH SERVICES PROGRAM AUDIT
FOR THE PERIOD OF JULY 1, 2001 THROUGH JUNE 30, 2005**

Summary

The State Controller's Office audited the costs claimed by County for the legislatively mandated SED Pupils: Out of State Mental Health Services Program for the period of July 1, 2001 through June 30, 2005. The County claimed \$9,933,677 for the mandated program, and the State found \$7,647,539 is allowable and \$2,286,138 is unallowable. The State alleges that the unallowable costs occurred because the County claimed ineligible vendor payments for out-of-state residential placement of SED pupils in facilities that are owned and operated for profit and because the County claimed unallowable travel costs. The State has broken down the unallowable costs claimed into two findings. The County disputes both of the findings and asserts that the entire amount claimed less the amount the State has already paid the County is the true allowable amount of costs.

The County disputes Finding 1 – unallowable vendor payments - because the California Code of Regulations section 60100(h) and Welfare and Institutions Code section 11460(c)(3) cited by the State are in conflict with provisions of federal law, including the Individuals with Disabilities Education Act (IDEA) and Section 472(c)(2) of the Social Security Act (42 U.S.C. 672 (c)(2)). In addition, the claim years of July 1, 2001 through June 30, 2004 have already been adjudicated in *County of San Diego, et al. v. State of California*. In the *San Diego* case, the counties prevailed and have a court ruling specifically citing amounts that the State must reimburse the County. Please see judgment attached hereto as Exhibit A and the following argument in support of County's response to Finding 1.

The County disputes Finding 2 – unallowable travel costs. The State asserts that the County failed to provide sufficient documentation to show that the travel costs claimed were traceable to source documents that show evidence of the validity of the costs and their relationship to the state mandated program. The County asserts that it has a consistent cost allocation methodology that it will demonstrate below that clearly shows that the \$49,164 claimed are true unduplicated costs that should be allowed.

Response To Finding 1 - Unallowable Vendor Payments

The State's position is that the County claimed unallowable vendor costs of \$2,236,974 for the audit period; and the County disputes this finding. The County specifically disputes the finding that it claimed ineligible vendor payments of \$1,979,388 (board and care costs of \$972,392 and treatment costs of \$1,006,996) for out-of-state residential placement of SED pupils owned and operated for profit. In support of its position, the State cites the California Code of Regulations, Title 2, section 60100, subdivision (h), which provides that out-of-state residential placements will be made only in residential programs that meet the requirements of Welfare and Institutions Code section 11460(c)(2) through (3). Welfare and Institutions Code section 11460(c) (3) provides that reimbursement will only be paid to a group home organized and operated on a nonprofit basis.

The County asserts that it is entitled to the entire amount claimed less the sum already paid by the State. Please see Summary of Program Costs – SED Claims – July 1, 2001 - June 30, 2005 attached hereto as Exhibit B. In support of its position, the County provides the following five arguments and Exhibits A through D attached hereto. The first argument is primary for the claim years July 1, 2001 through June 30, 2004, and arguments 2-5 are made in the alternative. For the claim year July 1, 2004 through June 30, 2005, arguments 2-5 shall be considered primary.

1. The Court Ruling in *County of San Diego, et al. v. State of California, et al.* (Case No. 825109 Consolidated with Case No. 827845) Clearly States the Amount the State Owes the County for the Claim Years July 1, 2001 Through June 30, 2004.

The County of San Diego has a judgment in the above-referenced matter that states the amount that the State owes the County for the claim years July 1, 2001 through June 30, 2004. Please see Judgment, Writ and Claims Summary – San Diego attached hereto as Exhibit A. It is clear from that judgment that the County is owed the entire amount it claimed for the audit period. The County prevailed in the *San Diego* case and while an appeal is pending, the State cannot use this forum to try to amend the judgment. Therefore, for the claim years July 1, 2001 through June 30, 2004, the amount owed the County is \$8,071,798 and cannot be amended here. Please see Summary of Program Costs – SED Claims – July 1, 2001 - June 30, 2005 attached hereto as Exhibit B.

2. California Law Prohibiting For-Profit Placements is Inconsistent with Both Federal Law, Which No Longer Has Such a Limitation, and With IDEA's "Most Appropriate Placement" Requirement.

In 1990, Congress enacted IDEA (20 U.S.C.S. § 1400-1487) pursuant to the Spending Clause (U.S. Const., Art. I, § 8, cl. 1). According to Congress, the statutory purpose of IDEA is "... to assure that all children with disabilities have available to them ... a free appropriate public education which emphasizes special education and related services designed to meet their unique needs. ..." 20 U.S.C. § 1400(d)(1)(A); *County of San Diego v. Cal. Special Educ. Hearing*, 93 F.3d 1458, 1461 (9th Cir. 1996).

To accomplish the purposes and goals of IDEA, the statute "provides federal funds to assist state and local agencies in educating children with disabilities but conditions such funding on compliance with certain goals and procedures." *Ojai Unified School Dist. v. Jackson*, 4 F.3d 1467, 1469 (9th Cir. 1993); see *Ciresoli v. M.S.A.D. No. 22*, 901 F. Supp. 378, 381 (D.Me. 1995). All 50 states currently receive IDEA funding and therefore must comply with IDEA. *County of L.A. v. Smith*, 74 Cal. App. 4th 500, 508 (1999).

IDEA defines "special education" to include instruction conducted in hospitals and institutions. If placement in a public or private residential program is necessary to provide special education, regulations require that the program must be provided at no cost to the parents of the child. 34 C.F.R. § 300.302 (2000). Thus, IDEA requires that a state pay for a disabled student's residential placement when necessary. *Indep. Schl. Dist. No. 284 v. A.C.*, 258 F.3d

769 (8th Cir. 2001). Local educational agencies (LEA) initially were responsible for providing all the necessary services to special education children (including mental health services), but Assembly Bill 3632/882 shifted responsibility for providing special education mental health services to the counties.

Federal law initially required residential placements to be in nonprofit facilities. In 1997, however, the federal requirements changed to remove any reference to the tax identification (profit/nonprofit) status of an appropriate residential placement as follows: Section 501 of the Personal Responsibility and Work Opportunity Responsibility Act of 1996 states, Section 472(c)(2) of the Social Security Act (42 U.S.C. 672(c)(2) is amended by striking "nonprofit." That section currently states:

The term "child-care institution" means a private child-care institution, or a public child-care institution which accommodates no more than twenty-five children, which is licensed by the State in which it is situated or has been approved, by the agency of such State responsible for licensing or approval of institutions of this type, as meeting the standards established for such licensing, but the term shall not include detention facilities, forestry camps, training schools, or any other facility operated primarily for the detention of children who are determined to be delinquent.

The California Code of Regulations, Title 2, section 60100, subdivision (h) and Welfare and Institutions Code section 11460(c)(2) through (3) are therefore inconsistent with the Social Security Act as referenced above, as well as inconsistent with a primary principle of IDEA as described below.

IDEA "was intended to ensure that children with disabilities receive an education that is both appropriate and free." *Florence County School District Four v. Carter*, 510 U.S. 7, 13, 126 L. Ed. 2d 284, 114 S. Ct. 361 (1993). A "free appropriate public education" (FAPE) includes both instruction and "related services" as may be required to assist a child with a disability. 20 U.S.C. § 1401 (22). Both instruction and related services, including residential placement, must be specially designed to suit the needs of the individual child. 20 U.S.C. § 1401(25). The most appropriate residential placement specially designed to meet the needs of an individual child may not necessarily be one that is operated on a nonprofit basis. Consequently, to limit the field of appropriate placements for a special education student would be contrary to the FAPE requirement referenced above. Counties and students cannot be limited by such restrictions because the most appropriate placement for a student may not have a nonprofit status. This need for flexibility becomes most pronounced when a county is seeking to place a student in an out-of-state facility which is the most restrictive level of care. Such students have typically failed California programs and require a more specialized program that may not necessarily be nonprofit.

In contrast to the restrictions placed on counties with respect to placement in nonprofits, LEAs are not limited to accessing only nonprofit educational programs for special education students. When special education students are placed in residential programs, out-of-state LEAs may utilize the services provided by certified nonpublic, nonsectarian schools and agencies that

are for profit. See Educ. Code § 56366.1. These nonpublic schools become certified by the state of California because they meet the requirements set forth in Education Code sections 56365 *et seq.* These requirements do not include nonprofit status, but rather, among other things, the ability to provide special education and designated instruction to individuals with exceptional needs which includes having qualified licensed and credentialed staff. LEAs monitor the out-of-state nonpublic schools through the Individualized Education Program process and are also required to monitor these schools annually which may include a site visit. Consequently, counties and LEAs should not be subject to different criteria when seeking a placement in out-of-state facilities for a special education student. Consistent with federal law, counties must have the ability to place students in the most appropriate educational environment out-of state and not be constrained by nonprofit status.

3. Parents can be Reimbursed When Placing Students in Appropriate For-Profit Out-of-State Facilities. County Mental Health Agencies will be Subject to Increased Litigation Without the Same Ability to Place Seriously Emotionally Disturbed Students in Appropriate For-Profit Out-of-State Facilities.

In *Florence County School District Four, et al. v. Shamon Carter*, 510 U.S. 7, 114 S.Ct. 361 (1993), the U.S. Supreme Court found that although the parents placed their child in a private school that did not meet state education standards and was not state approved, they were entitled to reimbursement because the placement was found to be appropriate under IDEA. The parents in *Carter* placed their child in a private school because the public school she was attending provided an inappropriate education under IDEA.

In California, if counties are unable to access for profit out-of-state programs, they may not be able to offer an appropriate placement for a child that has a high level of unique mental health needs that may only be treated by a specialized program. If that program is for profit, that county will therefore be subject to potential litigation from parents who through litigation may access the appropriate program for their child regardless of for profit or nonprofit status.

County Mental Health Agencies recommend out-of state residential programs for special education students only after in state alternatives have been considered and are not found to meet the child's needs. See Gov't Code §§ 7572.5 and 7572.55. As described in 7572.5 and 7275.55, such decisions are not made hastily and require levels of documented review, including consensus from the special education student's individualized education program team. Further, when students require the most restrictive educational environment, their needs are great and unique. Consistent with IDEA, counties should be able to place special education students in the most appropriate program that meets their unique needs without consideration for the programs for profit or nonprofit status so that students are placed appropriately and counties are not subject to needless litigation.

4. County Contracted with Nonprofit Out-of-State Residential Program for SED Pupils.

During the audit period, the County contracted with Mental Health Systems, Inc. (Provo Canyon School) the provider of the out-of-state residential services that are the subject of the proposed disallowance that the County disputes in this Response. As referenced in the April 28, 2007 letter from the Internal Revenue Service (attached hereto as Exhibit C) Mental Health Systems, Inc. (Provo Canyon School) is a nonprofit entity. The County contracted with this provider in a manner consistent with the requirements of the California Code of Regulations and Welfare and Institutions Code referenced above. The State never provided any guidance to counties as to how to access or contract with appropriate out-of-state facilities that meet State criteria or qualifications. The State never provided counties a list of appropriate out-of-state facilities that meet State requirements. County should not be penalized now for fulfilling the requirements of the law with little or no guidance from the State.

5. There are no Requirements in Federal or State law Regarding the Tax Identification Status of Mental Health Treatment Services Providers. Thus, there are no grounds to disallow the County's Treatment Costs.

Government Code section 7572 (c) provides that "Psychotherapy and other mental health assessments shall be conducted by qualified mental health professionals as specified in regulations developed by the State Department of Mental Health in consultation with the State Department of Education. . . ." The California Code of Regulations Title 2, Division 9, Chapter 1, Article 1, Section 60020 (i) and (j) further describe the type of mental health services to be provided in the program as well as who shall provide those services to special education pupils. There is no mention that the providers have a nonprofit or for profit status. The requirements are that the services "shall be provided directly or by contract at the discretion of the community mental health service of the county of origin" and that the services are provided by "qualified mental health professionals." Qualified mental health professionals include licensed practitioners of the healing arts such as: psychiatrists, psychologists, clinical social workers, marriage, family and child counselors, registered nurses, mental health rehabilitation specialists and others who have been waived under Section 5751.2 of the Welfare and Institutions Code. The County has complied with all these requirements. Consequently, because there is no legal requirement that treatment services be provided by nonprofit entities the State cannot and shall not disallow the treatment costs.

Response To Finding 2 - Unallowable Travel Costs

The State alleges that the County has claimed unallowable travel costs of \$49,164 for the audit period July 1, 2001 through June 30, 2005. The County disputes this finding and submits the attached cost per unit calculation as Exhibit D. This cost per unit calculation clearly indicates that the County has excluded the travel costs in calculating the cost per unit per claim to calculate the gross costs in the County's Handicapped and Disabled Student's claim. Therefore, because these costs were clearly excluded they are valid SED claimable costs in the amount of \$49,164.00.

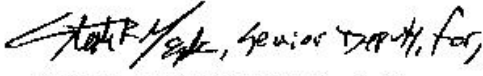
Conclusion

In conclusion, the County asserts that the costs of \$8,057,183 as set forth in Exhibit B should be allowed.

Dated: November 2, 2007

Respectfully submitted,

JOHN J. SANSONE, County Counsel

By  *Lisa M. Macchione, Senior Deputy, for,*

LISA M. MACCHIONE, Senior Deputy
Attorneys for the County of San Diego

F I L E D
Clerk of the Superior Court

MAY 12 2005

By: L. ROCKWELL, Deputy

IN THE SUPERIOR COURT OF THE STATE OF CALIFORNIA

IN AND FOR THE COUNTY OF SAN DIEGO

COUNTY OF SAN DIEGO,

Plaintiff/Petitioner,

v.

STATE OF CALIFORNIA; STEVE
WESTLY in his official capacity as California
State Controller; PHIL. ANGELIDES in his
official capacity as California State Treasurer;
DONNA ARDUIN in her official capacity as
Director of the California State Department of
Finance; and DOES 1 through 50, inclusive,

Defendants/Respondents.

Case No. GIC 825109 (consolidated with
Case No. GIC 827845)

JUDGMENT (PROPOSED)

Trial Date: November 28, 2005
Time: 10:30 a.m.
Dept: 70
I/C Judge: Honorable Jay M. Bloom
Actions filed: 2/3/04 and 4/1/04

JUDGMENT (PROPOSED)

EXHIBIT A-1

1 COUNTY OF ORANGE,
2 Plaintiff/Petitioner,
3 v.
4 STATE OF CALIFORNIA; STEVE
5 WESTLY in his official capacity as California
6 State Controller; PHIL ANGELES in his
7 official capacity as California State Treasurer;
8 DONNA ARDUIN in her official capacity as
9 Director of the California State Department of
10 Finance; and DOES 1 through 50, inclusive,
11 Defendants/Respondents.

12 Plaintiffs/Petitioners County of San Diego's and County of Orange's consolidated
13 complaints for declaratory relief and petitions for issuance of a writ of mandate came on for trial
14 on November 28, 2005, at 10:30 am., in Department 70 of the above-entitled court, the
15 Honorable Jay M. Bloom, judge presiding. The County of San Diego was represented by John
16 J. Sansone, County Counsel by Timothy M. Barry, Senior Deputy. The County of Orange was
17 represented by Benjamin P. de Mayo, County Counsel by Wendy J. Phillips, Deputy County
18 Counsel. The State of California, California State Controller, California State Treasurer, and
19 Director of the California State Department of Finance, were represented by William Lockyer,
20 Attorney General by Leslie R. Lopez, Deputy Attorney General.

21 Having heard and considered the evidence both written and oral and the oral arguments
22 of counsel for the parties it is hereby ORDERED, AJUDGED and DECREED as follows:

23 1. The State of California is obligated to reimburse the County of San Diego and the
24 County is entitled to judgment in the total principal sum of \$41,652,974 for the balance due on
25 its claims for costs incurred in providing State mandated programs and services from fiscal year
26 1994-95 through fiscal year 2003-04, together with interest thereon at the legal rate of seven
27

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JUDGMENT (PROPOSED)

EXHIBIT A-2

1 percent (7%) per annum from February 3, 2004. Interest on the \$41,652,974 at the legal rate
2 from February 3, 2004, through May 10, 2006 (826 days), the date of entry of this judgment, is
3 \$6,328,236 for a total judgment of \$47,981,210.

4 2. The State of California is obligated to reimburse the County of Orange and the
5 County is entitled to judgment in the total principal sum of \$72,755,977 for the balance due on
6 its claims for costs incurred in providing State mandated programs and services from fiscal year
7 1994-95 through fiscal year 2003-04, together with interest at the legal rate of seven percent
8 (7%) per annum from April 1, 2004. Interest on the \$72,755,977 at the legal rate from April 1,
9 2004, through May 10, 2006 (770 days), the date of entry of this judgment, is \$9,982,132 for a
10 total judgment of \$82,738,109.

11 3. The Counties request for pre-petition interest is denied.

12 4. A writ of mandate pursuant to Code of Civil Procedure section 1084, et seq. shall
13 issue commanding respondents, State of California, State Controller, State Treasurer, and
14 Director of the California State Department of Finance to pay the amount of the judgment plus
15 interest to the County of San Diego and the County of Orange over the fifteen year period
16 required by Government Code section 17617 (or a shorter period if the Legislature enacts a
17 shorter period, elects to pay the debt off earlier or is otherwise required by law to pay the debt
18 off over a shorter period) in equal annual installments beginning with the budget for the 2006-07
19 fiscal year and annually thereafter each successive budget until paid.

20 5. Respondents will file a return on the writ with the court within 90 days of the
21 enactment of the State budget for each fiscal year commencing with the 2006-07 fiscal year
22 demonstrating compliance with the writ until the amounts owed have been fully paid.

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1 6. This court will retain jurisdiction to enforce the writ in the event respondents fail
2 to comply with the writ.

3 7. Petitioners/plaintiffs are awarded costs of suit in the amount of \$ _____.

4
5 DATED: MAY 12 2006

JAY M. BLOOM

JUDGE OF THE SUPERIOR COURT

6
7 APPROVED AS TO FORM AND CONTENT,

8 BILL LOCKYER, Attorney General

9 By

10 LESLIE R. LOPEZ, Deputy Attorney General
11 for Defendants State Of California, Steve Westly,
Phil Angelides, and Tom Campbell

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JUDGMENT (~~PROPOSED~~)

EXHIBIT A-4

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8 **IN THE SUPERIOR COURT OF THE STATE OF CALIFORNIA**
9 **IN AND FOR THE COUNTY OF SAN DIEGO**

10 COUNTY OF SAN DIEGO,
11 Plaintiff/Petitioner,

12 v.

13 STATE OF CALIFORNIA; STEVE
14 WESTLY in his official capacity as California
15 State Controller; PHIL ANGELIDES in his
16 official capacity as California State Treasurer;
17 DONNA ARDUIN in her official capacity as
18 Director of the California State Department of
19 Finance; and DOES 1 through 50, inclusive,

20 Defendants/Respondents.

Case No. GIC 825109 (consolidated with
Case No. GIC 827845)

WRIT (~~PROPOSED~~)

Trial Date: November 28, 2005
Time: 10:30 a.m.
Dept: 70
I/C Judge: Honorable Jay M. Bloom
Actions filed: 2/3/04 and 4/1/04

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WRIT (~~PROPOSED~~)

EXHIBIT A-5

1 COUNTY OF ORANGE,

2 Plaintiff/Petitioner,

3 v.

4 STATE OF CALIFORNIA; STEVE
5 WESTLY in his official capacity as California
6 State Controller; PHIL ANGELIDES in his
7 official capacity as California State Treasurer;
8 DONNA ARDUIN in her official capacity as
9 Director of the California State Department of
Finance; and DOES 1 through 50, inclusive,

10 Defendants/Respondents.

11 TO: Respondents State of California, California State Controller, California State
12 Treasurer, and the California State Department of Finance and its current and future directors,
13 together with their agents, employees and successors in interest:

14 The court having ordered that a writ of mandate be issued:

15 **UPON RECEIPT OF THIS WRIT, YOU ARE HEREBY COMMANDED TO DO
16 THE FOLLOWING:**

17 1. Pay the judgment in favor of the County of San Diego in the amount of
18 \$47,981,210 together with court ordered costs, plus interest at the rate of 7% per annum from
19 the date of entry of judgment, for the balance due on its claims for costs incurred in providing
20 State mandated programs and services from fiscal year 1994-95 through fiscal year 2003-04,
21 over the fifteen year period required by Government Code section 17617 (or a shorter period if
22 the Legislature enacts a shorter period, elects to pay the debt off earlier or is otherwise required
23 by law to pay the debt off over a shorter period) in equal annual installments beginning with the
24 budget for the 2006-07 fiscal year and annually thereafter from each successive budget until the
amounts owed with interest are paid in full.

25 2. Pay the judgment in favor of the County of Orange in the amount of \$82,738,109
26 together with court ordered costs, plus interest at the rate of 7% per annum from the date of
27 entry of judgment, for the balance due on its claims for costs incurred in providing State
28 mandated programs and services from fiscal year 1994-95 through fiscal year 2003-04, over the

1
WRIT (~~PROPOSED~~)

EXHIBIT A-6

1 fifteen year period required by Government Code section 17617 (or a shorter period if the
2 Legislature enacts a shorter period, elects to pay the debt off earlier or is otherwise required by
3 law to pay the debt off over a shorter period) in equal annual installments beginning with the
4 budget for the 2006-07 fiscal year and annually thereafter from each successive budget until the
5 amounts owed with interest are paid in full.

6 3. File a return on the writ with the court within 90 days of the enactment of the State
7 budget for each fiscal year commencing with the 2006-07 fiscal year demonstrating compliance
8 with this writ until the amounts owed have been fully paid.

9
10 By: *L. Rockwell*
11 DEPUTY CLERK **L. Rockwell**

12 LET THE FOREGOING WRIT ISSUE

13
14 DATED: MAY 12 2006

[Signature]
15 JUDGE OF THE SUPERIOR COURT

16 APPROVED AS TO FORM AND CONTENT

17 BILL LOCKYER, Attorney General

18 By
19 LESLIE R. LOPEZ, Deputy Attorney General
20 for Defendants State Of California, Steve Westly,
21 Phil Angelides, and Tom Campbell

Clairius Summary - San Diego

ITEM - STATE DEPARTMENT Mandate	FY 94-95	FY 95-96	FY 96-97	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02	FY 02-03	FY 03-
	Protocols (Ch 955/89)							29,726		
By Local Health Officers (Ch 268/91)								24,135	31,052	22,352
0001 Department of Developmental										
(Ch 1304/80)								1,549	5,790	6,1
y Disabled: Attorney Services (Ch										
Retarded: Diversion (Ch 1253/80)										
0001 Department of Mental Health										
y Disordered Sex Offenders) (Ch 1036/78 & Ch 991/79))								4,899	3,118	
ered Offenders' Extended Commitment 1418/85)						22,037	19,150	27,765	24,456	33,0
ason Of Insanity (Ch 1114/79 and Ch						40,048		73,605	77,247	84,3
onally Disturbed Pupils: Out-Of-State ervices (Ch 654/96)				102,351	515,963	1,085,657	1,135,792	1,691,153	4,450,120	2,485,0
licapped and Disabled Students (Ch 1274/85)						440,448	857,575	5,401,433	7,270,033	1,705,6

Summary of Program Costs
SED Claims - July 1, 2001 - June 30, 2005

<u>Cost Elements</u>	<u>Actual Costs Claimed</u>	<u>Allowable</u>	<u>Adjustments</u>	<u>Remarks</u>
<u>July 1, 2001 - June 30, 2002</u>				
Ongoing Costs - Mental Health Service:				
Vendor Reimbursements	\$ 1,681,983	\$ 1,677,988	\$ (3,995)	Duplicated costs
Travel	9,170	9,170	-	
Total program costs	<u>\$ 1,691,153</u>	<u>\$ 1,687,158</u>	<u>\$ (3,995)</u>	
Less: Amount paid by State		-		
Allowable costs claimed in excess of amount paid		<u>\$ 1,687,158</u>		
<u>July 1, 2002 - June 30, 2003</u>				
Ongoing Costs - Mental Health Service:				
Vendor Reimbursements	\$ 4,435,895	\$ 4,216,894	\$ (218,701)	Ineligible in-State and clients' costs.
Travel	15,425	15,425	-	
Sub-Total program costs	<u>\$ 4,451,120</u>	<u>\$ 4,232,419</u>	<u>\$ (218,701)</u>	
Less: Late filing penalty	<u>\$ (1,000)</u>	<u>(1,000)</u>	<u>\$ -</u>	
Total Program Costs	<u>\$ 4,450,120</u>	<u>\$ 4,231,419</u>	<u>\$ (218,701)</u>	
Less: Amount paid by State		-		
Allowable costs claimed in excess of amount paid		<u>\$ 4,231,419</u>		
<u>July 1, 2003 - June 30, 2004</u>				
Ongoing Costs - Mental Health Service:				
Vendor Reimbursements	\$ 2,158,853	\$ 2,136,378	\$ (22,275)	Ineligible clients' costs
Travel	15,843	15,843	-	
Sub-Total program costs	<u>\$ 2,174,496</u>	<u>\$ 2,152,221</u>	<u>\$ (22,275)</u>	
Less: Late filing penalty	<u>\$ (1,000)</u>	<u>(1,000)</u>	<u>\$ -</u>	
Total Program Costs	<u>\$ 2,173,496</u>	<u>\$ 2,151,221</u>	<u>\$ (22,275)</u>	
Less: Amount paid by State		-		
Allowable costs claimed in excess of amount paid		<u>\$ 2,151,221</u>		
<u>July 1, 2004 - June 30, 2005</u>				
Ongoing Costs - Mental Health Service:				
Vendor Reimbursements	\$ 1,610,182	\$ 1,597,567	\$ (12,615)	Ineligible clients' costs
Travel	8,726	8,726	-	
Total program costs	<u>\$ 1,618,908</u>	<u>\$ 1,606,293</u>	<u>\$ (12,615)</u>	
Less: Amount paid by State		(1,618,908)		
Allowable costs claimed in excess of amount paid		<u>\$ (12,615)</u>		
<u>Summary July 1, 2001 - June 30, 2005</u>				
Ongoing Costs - Mental Health Service:				
Vendor Reimbursements	\$ 9,886,513	\$ 9,628,927	\$ (257,586)	
Travel	\$ 49,164	\$ 49,164	\$ -	
Sub-Total program costs	<u>\$ 9,935,677</u>	<u>\$ 9,678,091</u>	<u>\$ (257,586)</u>	
Less: Late filing penalty	<u>\$ (2,000)</u>	<u>(2,000)</u>	<u>\$ -</u>	
Total Program Costs	<u>\$ 9,933,677</u>	<u>\$ 9,676,091</u>	<u>\$ (257,586)</u>	
Less: Amount paid by State		(1,618,908)		
Allowable costs claimed in excess of amount paid		<u>\$ 8,057,183</u>		
Allowable per State Audit		6,028,631		
Difference - amount being appealed		<u>\$ 2,028,552</u>		
Breakdown:				
Treatment & R&B costs - for profit facilities		\$ 1,979,388		
Travel Costs		49,164		
Grand Total		<u>\$ 2,028,552</u>		

EXHIBIT B

Administration

MAY 07 2007

Internal Revenue Service

Date: April 26, 2007

MENTAL HEALTH SYSTEMS INC
9465 FARNHAM ST
SAN DIEGO CA 92123

Department of the Treasury
P. O. Box 2508
Cincinnati, OH 45201

Person to Contact:
T. Buckingham 29-70700
Customer Service Representative
Toll Free Telephone Number:
877-828-5600
Federal Identification Number:
95-3302967

Dear Sir or Madam:

This is in response to your request of April 26, 2007, regarding your organization's tax-exempt status.

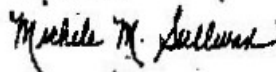
In November 1982 we issued a determination letter that recognized your organization as exempt from federal income tax. Our records indicate that your organization is currently exempt under section 501(c)(3) of the Internal Revenue Code.

Our records indicate that your organization is also classified as a public charity under section 509(a)(2) of the Internal Revenue Code.

Our records indicate that contributions to your organization are deductible under section 170 of the Code, and that you are qualified to receive tax deductible bequests, devises, transfers or gifts under section 2055, 2106 or 2522 of the Internal Revenue Code.

If you have any questions, please call us at the telephone number shown in the heading of this letter.

Sincerely,



Michele M. Sullivan, Oper. Mgr.
Accounts Management Operations 1

EXHIBIT C

SB90 Cost Per Unit Calculation in the HDS Claims

This spreadsheet demonstrates that the County have excluded the Travel Costs in calculating the cost per unit to calculate Gross Costs in the HDS claim and therefore are valid SED claimable costs. in the amount of \$ 49,164.00.

Fiscal Year 01-02							
	Gross Cost Per Cost Report	Less: Travel Costs	Adjusted Gross Cost	Total Units	Cost Per Unit	Cost Per Unit per Claim & as Audited	
Case Mgt	3,807,337	-	3,807,337	1,884,502	\$ 2.02	\$ 2.02	
MHS	5,932,422	(9,170)	5,923,252	4,381,913	\$ 1.35	\$ 1.35	
Medication	15,577,046	-	15,577,046	2,298,712	\$ 6.78	\$ 6.78	

Fiscal Year 02-03							
	Gross Cost Per Cost Report	Less: Travel Costs	Adjusted Gross Cost	Total Units	Cost Per Unit	Cost Per Unit per Claim & as Audited	
Case Mgt	3,198,545	-	3,198,545	2,045,546	\$ 1.56	\$ 1.56	
MHS	8,569,151	(15,425)	8,553,726	4,280,347	\$ 2.00	\$ 2.00	
Medication	14,843,828	-	14,843,828	2,475,945	\$ 6.00	\$ 6.00	

Fiscal Year 03-04							
	Gross Cost Per Cost Report	Less: Travel Costs	Adjusted Gross Cost	Total Units	Cost Per Unit	Cost Per Unit per Claim & as Audited	
Case Mgt	2,155,387	-	2,155,387	1,631,979	\$ 1.32	\$ 1.32	
MHS	9,573,387	(15,843)	9,557,544	3,565,746	\$ 2.68	\$ 2.68	
Medication	14,311,297	-	14,311,297	2,407,363	\$ 5.94	\$ 5.94	

Fiscal Year 04-05							
	Gross Cost Per Cost Report	Less: Travel Costs	Adjusted Gross Cost	Total Units	Cost Per Unit	Cost Per Unit per Claim & as Audited	
Case Mgt	4,070,095	-	4,070,095	1,201,820	\$ 3.39	\$ 3.39	
MHS	7,921,169	(8,726)	7,912,443	2,211,448	\$ 3.58	\$ 3.58	
Medication	15,556,190	-	15,556,190	2,094,018	\$ 7.43	\$ 7.43	

EXHIBIT D

**State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250-5874**

<http://www.sco.ca.gov>